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Court Questions FCC Authority To Sanction Comcast In Web Traffic Management Case

During oral arguments on Comcast's appeal of an FCC order that held the company liable for violations of the FCC's 2005 policy statement on net neutrality, the D.C. Circuit Court of Appeals cast doubt on the FCC's authority to sanction Comcast for blocking peer-to-peer (P2P) file transfers between users of the BitTorrent web site. One member of the three-judge panel told the FCC: "you have yet to identify a specific statute." In August 2008, the FCC decreed that Comcast's practice of throttling P2P file transfers between BitTorrent users during periods of network congestion constituted discriminatory conduct that violated the agency's 2005 net neutrality principles. Although the FCC did not impose a fine, it ordered Comcast to cease its file blocking practices and to revise its network management policies. The FCC maintained that its authority to hold Comcast liable for violations of the 2005 policy statement derives from the agency's ancillary jurisdiction under Title I of the 1934 Communications Act. Comcast challenged the FCC order on grounds that the 2005 policy guidelines lack the force of FCC regulations and that no FCC rules, therefore, were violated. Observers say that the court's decision in the closely-watched case could impact ongoing FCC efforts to codify the 2005 net neutrality principles as part of the FCC's rules. At Friday's hearing, counsel for Comcast stressed that, in briefs filed with the court, the FCC "has not said it enforced any law . . . just pure policy." As such, Comcast complained that it "had absolutely no notice that our conduct was regulated." While FCC General Counsel Austin Schlick argued that the FCC had relied on ancillary jurisdiction conferred by Title I and by sections of the Communications Act that pertain to service and charges, market entry barriers, advanced telecommunications and the screening or blocking of offensive material, Judge A. Raymond Randolph replied, "you have jurisdiction, but where is the statute?" Asserting that, "the question here is, is there statutory authority," Judge David Tatel observed, "if it is just a [policy] statement without any authority," the ancillary rule provisions quoted by the FCC cannot form the basis for the FCC's decision. The court is expected to issue its ruling in the case later this year. Declaring that "this case underscores the importance of the FCC's ongoing rulemaking to preserve the free and open Internet," FCC Chairman Julius Genachowski said, "I remain confident the Commission possesses the legal authority it needs."

American Cable Association, Other Groups Request Conditions On Comcast-NBC Merger

Twenty five cable, satellite television and consumer groups led by the American Cable Association (ACA) wrote to President Obama and to members of Congress to seek strict conditions on Comcast's planned \$30 billion acquisition of NBC Universal (NBCU). These entities fear that the merger will result in higher prices and fewer choices for

IN THIS ISSUE:

- **Court Questions FCC Authority To Sanction Comcast In Web Traffic Management Case** [read more](#)
- **American Cable Association, Other Groups Request Conditions On Comcast-NBC Merger** [read more](#)
- **House Lawmaker Seeks Closure Of Tax Loophole That Facilitated Verizon-Fairpoint Deal** [read more](#)
- **Investor Groups Say Deregulation Can Boost Media Sector** [read more](#)
- **Orange, T-Mobile Request EC Approval Of British Wireless Venture** [read more](#)
- **Hutchison Whampoa To Take Hong Kong Phone Unit Private** [read more](#)

multichannel video subscribers and in restricted access to programming required by competitors of the merged entity. The Satellite Broadcasting & Communications Association, the National Telecommunications Cooperative Association, Free Press, the Consumers Union and the Organization for the Promotion and Advancement of Small Telecommunications Companies were included among the signers of the letter delivered late last week. Announced last month, the proposed merger of Comcast—the nation’s top cable system operator—and NBCU would create the largest producer and distributor of video programming in the nation, with control of two broadcast networks (NBC and Telemundo), 26 television broadcast stations, ten regional sports networks and a variety of national cable channels. Arguing that Comcast-NBCU would “become the country’s most powerful online and traditional programming company,” ACA and the other parties charged that the merged entity “would have strong incentives to discriminate against other multichannel video providers in granting access to its wealth of programming . . . as well as the market power to enforce anticompetitive ‘bundling.’” The parties further warned that, “driven by the need to increase cash flow and net income, Comcast-NBCU would have the incentive and ability to use its powerful array of media assets to compel competitors to pay more for programming than they should, especially in the area of retransmission consent for NBC broadcast stations.” The FCC and Justice Department are expected to take up to a year or more to review the deal.

House Lawmaker Seeks Closure Of Tax Loophole That Facilitated Verizon-Fairpoint Deal

Arguing that a tax loophole used by Verizon Communications in its 2007 sale of New England landlines to Fairpoint Communications saddled Fairpoint with enough debt to force Fairpoint into bankruptcy, Representative Paul Hodes (D-NH) introduced legislation that would repeal the Reverse Morris Trust provisions used by Verizon and other companies to avoid payment of capital gains taxes that stem from corporate mergers. Signed into law by President Clinton in 1997, the Reverse Morris Trust law exempts sellers in a merger transaction from paying capital gains taxes if shareholders from the selling firm retain a majority of shares in the post-merger entity. Although the Reverse Morris Trust enabled Verizon to save an estimated \$300 million in taxes that otherwise would have accrued from the Fairpoint transaction, the deal left Fairpoint with a debt load of \$1.7 billion. Fairpoint sought Chapter 11 bankruptcy protection last October. Critics have voiced similar concerns about Verizon’s pending sale of rural landlines in West Virginia and 13 other states to Frontier Communications. Verizon is expected to save \$600 million in taxes through that transaction. While acknowledging that a repeal of the Reverse Morris Trust law could bring “significant” amounts of revenue to the U.S. government, Hodes stressed that his motive in introducing the bill is to promote consumer fairness, as he maintained: “saddling small companies with a huge amount of debt creates real problems for consumers.” Noting that the Reverse Morris Trust has “nothing to do with the protection of phone service and poses no threat to phone customers,” a Verizon spokesman replied, “there is no public policy reason to change this law.”

Investor Groups Say Deregulation Can Boost Media Sector

At a workshop on media ownership conducted by the FCC on Tuesday, representatives of various investor and analyst groups spoke of the benefits of deregulation in boosting the viability of U.S. broadcasters that have struggled recently in the midst of a laggard economy and declining ad revenues. As FCC Media Bureau Chief Bill Lake confirmed that staffers are “formulating” a notice of inquiry on the agency’s media ownership rules “which we hope to do as early this year as we can,” industry analysts attending the workshop argued that the time of large-scale media consolidation is past as declining revenues and rising debt have induced many investors to pull out of the industry. In reply to Associate Media Bureau Chief Sarah Whitesell, who asked “what will it take for investors to embrace this industry again,” Brian Rich, the managing partner of media investment firm Catalyst Investors, said, “you want to try to figure out how to return the sector to growth,” as “investors . . . like businesses that are going up.” To spur such growth, most panelists agreed that relaxed restrictions on broadcast-newspaper cross ownership and on the ownership of two TV stations in the same market would help, as Rich emphasized: “the regulatory environment during this next upcoming cycle can have a profound impact on the future of broadcasting.” Brandon Burgess, the CEO of Ion Media, agreed, as he observed that “regulation designed to ensure that traditional

outlets across various old media don't dominate yesterday's world does little to ensure that diverse, independent and innovative players have a fair and equitable chance to compete." One panelist, however—Terry Jones of Syncom Funds—cautioned against media deregulation, as he argued that such an approach "allows those who have resources, who have gotten those resources free from the Commission over the last 80-some years, to be able to buy up what's really important, which is spectrum."

Orange, T-Mobile Request EC Approval Of British Wireless Venture

Merger partners Orange and T-Mobile filed for European Commission (EC) approval of their proposed British wireless venture on Tuesday, as the companies' rivals and consumer groups in the United Kingdom (UK) called on Great Britain's Office of Fair Trading (OFT) to request transfer of merger review to the UK. Announced in November, the proposed 50-50 joint venture would leapfrog current market leader O2 as the largest mobile phone operator in the UK with 28.4 million customers and a market share of 37%. The combined entity would also control more than 84% of available 1800 MHz band spectrum that is earmarked in the UK for advanced, high-speed wireless services. The filing of merger documents with the EC triggers the start of the EC's review timetable, under which the EC is required to hand down its initial ruling on February 15. On that date, the EC may approve the deal or launch an in-depth investigation that would take up to 90 days to complete. Meanwhile, the OFT confirmed Tuesday that it is considering "whether to make a request to the EC for the proposed joint venture to be referred to the OFT for review." Voicing concern about the impact of the proposed merger on competition, O2 and other opponents have urged the OET to investigate the transaction. O2 and 3UK, the smallest of Great Britain's five current wireless operators, have also called on the joint venture to relinquish some of the 1800 MHz spectrum that they will amass through the merger on grounds that permitting one company to control such a large amount of 1800 MHz spectrum will "distort the market." Since current European Union merger regulations went into effect in 2004, the OFT has made four requests for the EC to take over merger review. The final decision on which regulatory body will conduct that review rests with the EC.

Hutchison Whampoa To Take Hong Kong Phone Unit Private

To facilitate renewed expansion into emerging foreign markets, Hutchison Whampoa has offered to privatize its Hong Kong phone unit, Hutchison Telecommunications International (HTI), in a cash deal valued at HK \$4.23 billion (US \$545 million). Under the proposal, announced last Friday, Hutchison Whampoa would repurchase the 40% of HTI stock it does not already own at HK \$2.20 per share, which represents a premium of 33% over HTI's last closing share price of HK \$1.65 before trading in HTI shares was suspended on January 4. At its peak three years ago, HTI was valued in excess of US \$12.3 billion. Since then, HTI has sold or spun off operations in India and other key foreign markets and has taken a substantial hit on its valuation. (Sources indicate that HTI was valued at just over \$1 billion in the days immediately preceding the buyout announcement.) Once privatization is complete, Hutchison Whampoa intends to focus its investments on the expansion of current HTI operations in Thailand, Indonesia, Sri Lanka and Vietnam.

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